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Implementation

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A. Overview

Alexandria's growth in the past decade is partially the result of planning and infrastructure investments, such as the Eisenhower and King Street Metrorail stations and the urban street grid, that were the result of both public and private investment. The build-out of the Plan area, the future Potomac Yard Metrorail station, land uses, street grid and associated infrastructure will enable long-term redevelopment for the City, similar to infrastructure investments and planning in the City decades ago. If the City implements all of the recommendations of the Plan, the City could capture a significant share of the projected regional growth. The Plan lays out an ambitious 20 to 30 year vision for Alexandria's North Potomac Yard.

It is important to understand the degree to which the implementation and infrastructure components of the Plan are interrelated and depend on one another for their success. The required infrastructure and development mustalso be carefully phased. The transportation and circulation through the site are based on the provision of a Metrorail station and dedicated transit. Without a Metrorail station, the Plan does not work and is not feasible. The success of the residential neighborhoods will depend on the viable retail and commercial uses which will provide convenient access to goods and services. Open space and design excellence add value but will also add amenities for the workers, residents, and visitors. Without all of the necessary infrastructure improvements and amenities working together and phased appropriately, potential tenants, residents, and retail patrons will go somewhere that does provide the desired level of infrastructure improvements and amenities.

This chapter incorporates the planned land use and density, infrastructure, transportation, amenities, community facilities, phasing, and fiscal impacts. The implementation chapter serves several purposes that include:

- Evaluate the overall financial feasibility of the land use plan;
- Understand and describe the project economics and general financing concepts;
- Understand and describe the basic financial transaction structure between the City and developers contributions;
- Ensure that private development provides funding for public improvements and their on-going maintenance; and
- Finding the right balance of private and public funding that is needed to construct the Metrorail station.

B. Infrastructure, Amenities, and Phasing

The cost to construct a new WMATA Metrorail station is approximately $220 to $235 million (2015 dollars) for the A and B Metrorail station options discussed within the Plan. In addition, $16 million dollars in construction costs are anticipated for the dedicated transitway, with an additional $5 million anticipated for other transportation improvements. Transportation is not the only needed infrastructure given the number of employees, residents, visitors and students which will eventually reside, work or visit North Potomac Yard. Significant additional investment in sewer and water distribution and management are needed to accommodate the basic needs generated by the planned amount of development. In addition, services such as police, fire and schools will require services from the proposed development which are anticipated to be funded with a portion of the new taxes this project will generate.

The discussion of sources, uses and revenues below provides a static summary of total project financing, total project costs and total revenues. In actuality, these costs and revenues are incurred over time from the inception of development through the build-out of the project and the impacts of these timing issues have a potentially significant impact on the overall financial feasibility of the project. As is often the case with large, complex, urban infill redevelopment efforts, in the initial years of planning and constructing, a large proportion of overall costs must be incurred and revenues follow much later. At North Potomac Yard this is particularly true as a result of the significant infrastructure improvements, such as the Metrorail station, that must be made in the early phases to support development.

C. Zoning and Development Conditions

The City's Zoning Ordinance is its key regulatory tool, and is used to direct the size, character, use, and location of development throughout the City. A new Coordinated Development District is planned for Landbay F and recommends a rezoning for the Plan area.

The proposed increase in allowable development from 600,000 square feet to approximately 7.5 million square feet will require significant investment from the developer for infrastructure and facilities and amenities to meet public needs. The following are some of the site plan requirements for the City, which are generally included in the development special use permit process:

- Street and Street Improvements – Sidewalks – Street right-of-way (necessary to serve the needs of the site);
- Applicable Utilities such as Sanitary and Storm Sewer – Water – Electric (necessary to serve the needs of the site);
- Parks – Open Space (necessary to serve the site);
- Voluntary Affordable Housing Contribution;
- Voluntary Public Art Contribution (policy under development);
- High Quality Architecture and Streetscape;
- Underground Parking; and
- Sanitary Sewer and Stormwater.

In addition, in order for the development proposed in the Plan to be implemented, the following major transportation infrastructure improvements are required:

- WMATA Metrorail Station; and
- Dedicated High-Capacity Transitway.

The Plan recommends a number of other community benefits, desired by the City and community, be provided at additional cost to the developer, some of which include the following:

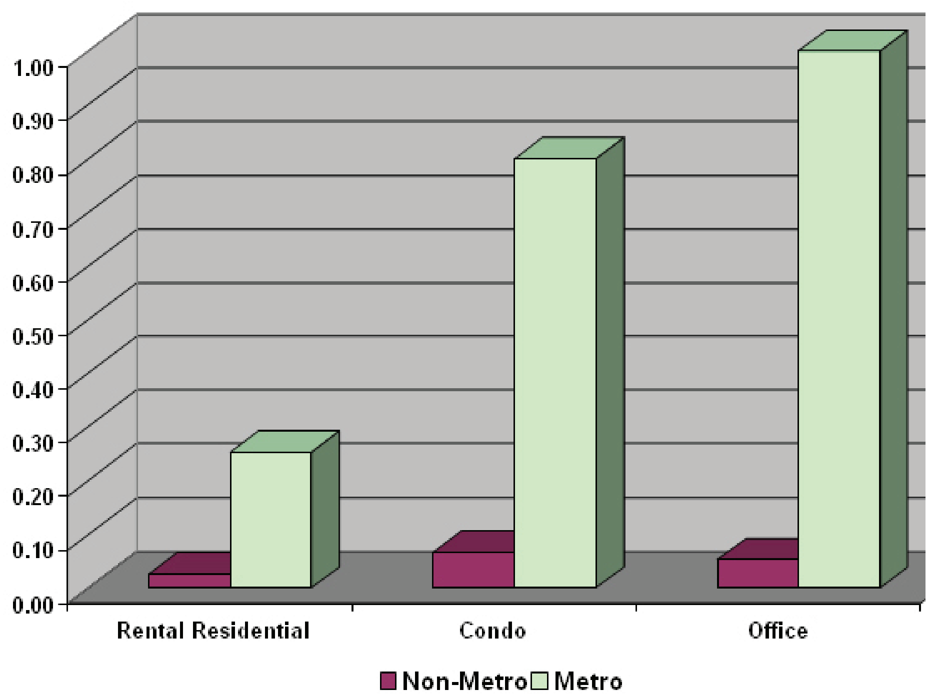
- Reservation for future school;
- Civic Uses – Performing Arts Theatre, etc; and
- Green – Sustainable Building Elements.

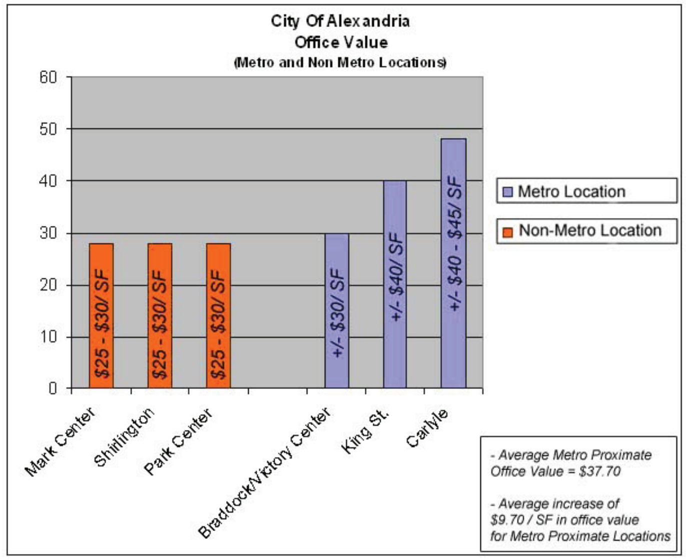
The developer's ability to invest in community benefits is driven by the strength of the market (i.e. achievable rents and revenues) and development costs. Although Potomac Yard is in a relatively strong market, there are significant costs associated with infrastructure development. In addition, because of the existing retail buildings and uses, redevelopment must generate enough income to pay development costs and achieve an adequate investment return to redevelop the existing buildings. When a return exceeds the return-on-cost threshold there is an opportunity for the developer to invest in public amenities.

The proposed rezoning would significantly increase the amount of density and associated value that could be provided to the City. The presence of a Metrorail station significantly increases potential public amenities by creating market value (higher rents) and reducing development cost (such as less parking required). (See Table 8). In addition, all other things being equal, absorption (the amount and pace of development) near Metrorail stations is faster than non-Metro locations. Office rents at Metrorail stations in Alexandria are almost one-and-a-half times greater than comparable non-Metrorail locations. (See Table 9). As such, the ability for the developer to contribute significantly toward public amenities increases significantly, almost tenfold, if a Metrorail station is constructed.

Table 8. Value Added by Presence of Metrorail Station

Table 9.Office Rents at Metrorail and Non-Metrorail Locations





While the current economic state of commercial real estate development makes a calculation speculative, accounting for developer cost and profit margin, by one conclusion, according to the City's consultants, W-ZHA the proposed increase in allowable development on the property with the construction of a new Metrorail station will increase the value of the land by as much as $240 million, creating value that can be spent toward community benefits. (See Table 10). The contribution amount will have to be refined as part of the implementation phase of the project.

Table 10. Increase in Value of Land Due to Increase in Allowable Development

2.5 FAR, Metro Office/Retail Mix Potomac Yard Retail Center			
	Existing Zoning	2.5 FAR	
Land Area (Sq. Ft.)	3,008,589	3,008,589	
FAR Feet	600,000	7,521,473	
Retail	600,000	20% - 1,504,295	
Office	0	80% - 6,017,178	
Retail			
Land Value	$90,000,000	$60,171,800	
Value /FAR Ft.		$40.00	
Office			
Land Value	$0	$270,773,000	
Value /FAR Ft.		$45.00	
			Difference
Total Value	$90,000,000	$330,944,800	$240,944,800
Discount for Profit			(10.00%) $216,850,300
Contribution / FAR Ft.			$28.83

Source: City of Alexandria; W-ZHA

D. Overview Of Financing The Potomac Yard Metrorail Station

The proposed rezoning of Landbay F increases the development on that landbay from 600,000 square feet of "big box" retail to 7,500,00 square feet of total development. The transportation network in this area of the City of Alexandria will not support this level of development, and thus the rezoning to this level of density cannot be approved, in the absence of the construction of a new Metrorail station and dedicated transit.

The Plan supports the recommendations of the Metrorail Station Feasibility Work Group (see final report Potomac Yard Metrorail Station Concept Development Study). In addition, the following fundamental principles should guide the City of Alexandria, its political decision makers, and staff:

- The City is supportive of the type of long-term, quality mixed-use development contemplated at Potomac Yard, and plans to provide the bond financing of the Metrorail station, but the financial risk to the City must be carefully structured and managed.
- The City plans to enact special tax districts on Landbays F, G, H, I, and J as well as Potomac Greens that will help pay for a portion of the cost of the Metrorail station, and to issue general obligation or other types of municipal bonds for such construction, most likely backed by the full faith and credit of the City of Alexandria, or a similar pledge.
- Special tax districts could be implemented as early as 2011 to help finance pre-construction and environmental study costs. At this time the needed tax rate prior has not been determined. Two special tax districts are contemplated: one district for the higher density Landbays F, G, and H, and a second tax district for the lower density Landbays I and J and Potomac Greens. The exact boundaries in Landbay H, I, and J remain to be determined.
- No negative cash impact on the City's General Fund in any given year. The projected "gap" between the anticipated tax revenues from the special tax district, per square foot developer contributions, plus additional incremental net new revenues generated by the project, will need to be "bridged" in the early years of the bond financing by firm and sufficient up front Landbay F guaranteed payments, so there will be no negative cash impact on the City's General Fund in any given year.
- Any proposed financing must be conservative with a sound financing structure and shared risk. The proposed financing must not put at risk the City's AAA/Aaa bond ratings, as well as projections used for the Metrorail station construction costs, as well as the project build-out timetable and resultant projected tax revenues need to utilize conservative assumptions, so that the downside risks can be minimized. Some of the downside risks also need to be shared by the participating parties.
- The final financing plan when approved by City must be based on final plans approved by the Washington Metropolitan Area Transit Authority and the City, and a guaranteed maximum or other fixed price construction contract for construction approved by WMATA must be in place for the station to be constructed and must be structured to minimize the possibility of cost overruns.
- Even with a combination of special tax districts, developer contributions, other contributions, and increased taxes, it is likely that if projections are not met, the City will have to pay any net shortfalls, and this risk and the impact on the City's ability to do other projects must be factored in to all proffer negotiations to result in a conservative, sound financing structure with shared risk.

Discussion

A plan of finance and agreement with the owner of North Potomac Yard (Landbay F) in regard to funding the $240 million (assumes for worst case financing modeling purposes the midpoint of a $210 million to $270 million construction range which is the B options with a 2015 construction midpoint and is also the highest cost of the three options A, B1 and B2 under consideration) Metrorail station to serve Potomac Yard and adjacent neighborhoods is a necessary precedent to any rezoning of Landbay F. Since the additional 7.5 million square feet of additional density of all types contemplated for Landbay F can only occur if the necessary transportation infrastructure (including a new Metrorail station) is provided, it must be certain that the station can be financed, constructed and put into operation.

Financing a $240 million project is an exceedingly difficult challenge given the enormity of this cost. In perspective, $240 million is nominally about two and one-half times the cost of the new T.C. Williams High School recently constructed in the City. Proof of the difficulty of this is that there has been only one new in fill Metrorail station (New York Avenue) constructed to date and added to the existing 103-mile Metrorail system that serves the entire Washington, D.C. area since the system was constructed starting in the 1970's. This is in large part due to the cost of such station additions, as well as the lack of significant federal and state funding opportunities for adding stations to existing subway systems. Also since individual stations largely benefit individual localities, the Washington Metropolitan Area Transit Authority (WMATA) does not spend its limited capital dollars on adding Metrorail stations to its system. In Virginia, where State transportation capital funding assistance to localities has collapsed, as the State's transportation tax revenues have fallen sharply and not kept up with demand, there also is no current significant new funding for mass transit capital projects such as a new Metrorail station. The absence of state and federal funding opportunities, leads to the conclusion that any Metrorail station within Potomac Yard must be planned to be almost entirely locally funded and financed, with any state and/or federal funding that might occur reducing that local funding burden.

Modeling of Financial Feasibility

To determine the financial feasibility of funding a Metrorail station, the City retained the transportation consulting firm of PB Consulting to undertake calculation of tax revenues potentially generated by the development of Potomac Yard, as well as modeling how City-issued general obligation bonds could raise the funds necessary to fund the construction of the station. These bonds would be serviced and repaid by a combination of developer contributions, net new taxes, as well as special tax district revenues.

The PB modeling made the following key revenue assumptions:

1. Tax rates assumed at 2009 levels and policies;
2. Special Tax District at 20-cents per $100 of valuation in the high density landbays;
3. As contemplated by the original Potomac Yard CDD approval, all of Potomac Yard (except the most southern Landbay L and Old Town Greens) including Potomac, Greens would be included in the Special Tax Districts and all net new tax revenues from those landbays (including already zoned Landbays G and H) counted as available revenues;
4. No current tax revenues generated by any Potomac Yard landbays would be counted as available for a Metrorail station financing;
5. Real Estate unit values (i.e., per unit or per square foot values) at 2009 values;
6. 10% value increase assumed for properties within ¼ mile of the Metrorail station entrance, with two entrances to the Metrorail station provided;

7. 6.5% (hotel) to 59.8% (residential) of new tax revenues (not including the $.20 per $100 special tax district revenues) would be assumed to be used to finance City and School services and capital costs to serve Potomac Yard and thus would not be available to assist in the Metrorail station financing;
8. 25-year straight-line build out of planned development starting in 2017, and
9. No federal or state aid assumed.

At the City's direction, PB consulting used the following key bond financing assumptions:

1. 30-year amortization of the bonds, commencing in 2014;
2. Use of AAA/Aaa rated general obligation bonds issued by the City;
3. Capitalized construction period interest, during the first three years;
4. A $275 million bond issuance ($240 million for construction, $30 million for capitalized interest during construction, and $5 million in related bond issuance costs);
5. Interest only repayment in years four, five and six; and
6. Gradual build-up of principal repayment in years seven through seventeen, and then level principal and interest through year thirty.

The results of the PB analysis shows that while there are sufficient net new tax revenues after 2024 to cover the debt service obligation of the Metrorail station bond financing, there is a significant up front gap from 2014 to 2024 (years one to eleven). This is because the net new tax revenues generated from development are projected not to grow sufficiently in the first eleven years after the bonds are issued (in part because the buildout of this order of magnitude of new development will be phased over the long term because of the limitations of market absorption). These projections are subject to many variables (actual station construction costs, land valuations, buildout timetable, interest costs, etc) and would need to be rerun and any financing plan adjusted accordingly to the realities of the time in which the decisions of going forward or not going forward with a Metrorail station would need to be made. For this reason, the final underwriting and construction contracting decisions must be based on final approved plans, not to exceed a construction contract price acceptable to the City and its advisors, as well as a sound and predictable financing plan.

Developer Contributions

To finance a portion of the Metrorail station ($475 million in total debt service over the 30-year period including $275 million in bonds and $200 million in interest) and to close the aforementioned funding gap, it will be necessary for the developers to agree to pay for a significant portion of the Metrorail station development that will benefit them by increasing the value of their property as well as accelerating when the market will facilitate the development of the property. Without such written agreement executed by the City with each of the three sets of owners (PYD, RREEF's institutional client, and MRP) or their successors, no Metrorail station can or will be built at Potomac Yard. In addition, the proposed density increase in North Potomac Yard/Landbay F of some 7.5 million square feet would not be able to be constructed, as the Metrorail station is precedent for any new development density in Landbay F as it is the only way that such density of that magnitude can receive adequate transportation capacity to function.

Developer agreements with the City need to recognize the different land use status of the various Landbays at Potomac Yard. For already developed property (Potomac Greens and The Station at Potomac Yard), there would be no developer conditions expected as development has already taken place. In particular the owners of Landbays G, H, I and J have contributed directly or indirectly to significant public infrastructure investment and land donation to the

City.
Those properties are proposed to be subject, however, (as was originally contemplated in the original Potomac Yard CDD approved by the City in 1999) to a special tax district levy.

It is contemplated that the high density special tax district (Landbays F, G, and H) would be put in place for 2011 at a 20¢ tax rate. It is also contemplated that the low density special tax district would be put in place in 2011, but with a 0¢ tax rate. That 0¢ tax rate would then be planned to be kept in place until the Metrorail station opened in 2017. Then after the Metrorail station has opened, the low density special tax district would have rate in the 5¢ to 10¢ tax range levied.

A $10 per square foot contribution for Metrorail can be justified as reasonable in that research has shown that the value of buildings within a quarter mile of a Metrorail station increase in value (i.e., in rents achieved) in comparison with similar properties not that close to a Metrorail station. If a property increases by 10% in long term value or about $40 per square foot, due to the presence of a Metrorail station within a quarter mile, it would be reasonable for the developers to pay $10 of that towards the costs of the Metrorail station.

For the owner of Landbay F, where any upzoning does not currently exist, and would only be approved as Metrorail station dependent, the developer contributions for the Metrorail station and for other public amenities should be significantly more than $10 per square foot, as the contemplated possible increase in approved overall density is 7.5 million square feet. As indicated earlier, the potential public increment of value through a rezoning alone (i.e, not including any long term value added from actual construction of higher density improvements) may be as much as $100 million to over $200 million. Given today’s unsettled commercial real estate markets, the determination of the value of a rezoning is challenging. A large portion of this public creation of private value should be allocated and committed towards the new Metrorail station and other infrastructure and public amenities upon which any rezoning will be dependent.

The timing of developer contributions would need to be negotiated and structured to fit the financing needs of the Metrorail station, and would have to be able to be financed by the developer in the commercial lending marketplace. Some of these funds should be paid up front and be sufficient to cover the estimated $32 million projected gap (PB December; 2009 Study) between projected revenues and projected debt service costs, and some of the funds paid at the time of the development. While paying up front for infrastructure puts a burden on the development project to be financed, it is a common real estate development practice.

It would not be unreasonable for the developer of North Potomac Yard/Landbay F to also commit a significant contribution for the transportation infrastructure – in this case a portion of the costs of the Metrorail station, as well as other public infrastructure. As of the time of the issuance of this chapter, the owners of North Potomac Yard/Landbay F have tentatively agreed to an up front shortfall guarantee in an amount that would be sufficient to close the projected funding gap. Negotiations with the City are active and on-going on this issue as well as that of other development conditions with many details to be worked out.

In addition to the developer contributions, there will have to be negotiations of the allocation of risk, and contingency plans and protections structured to cover circumstances that could arise prior to, during and after the Metrorail Station is constructed. Without such an executed agreement between the City and the owner of North Potomac Yard/Landbay F, on funding and related conditions, no new density authorization can be legally assumed to have been granted by the

City through the development and approval of this North Potomac Yard Plan, and therefore no new development could be initiated in Landbay F without a formal executed agreement and an actual rezoning (which is a distinct and separate action from an adoption of a North Potomac Yard Plan).

City Risks and Debt Policy Implications

While the financial model's projections and potential future agreements with developers in regard to their contributions could result in a plan of finance for the Metrorail station that is self-financing from developer contributions, special tax district revenues and net new tax revenues generated by that development, such projections are just projections and reality may be very different. Also City issuance of $275 million in bonds would represent a major, significant change in City debt policies and practices.

First, with regard to the model's projections and eventual reality, it is very difficult to predict real estate development. While real estate development is cyclical in nature, predicting the timing, length, highs and lows of real estate cycles is not possible. While many real estate pro forma projections proved correct, many real estate pro forma projections prove materially incorrect. The current real estate market place contains many examples of highly inaccurate projections and failed real estate ventures (such as development related local government issued “dirt bonds” that are now in default). While the use of general obligation financing would avoid a default situation, there is the real possibility that once the station was constructed that it would take far more time than the model projects for net new tax revenues to cover bond debt service obligations. This means that there is a risk that a deficit would occur and need to have a funding source. While some of this down side risk to the City and its General Fund may be able to be shared with the developer of Landbay F, it will be the City that is standing behind any bonds issued and would be the City's responsibility as the final backstop and ultimate obligator to pay debt service as it becomes due. Failure to repay the bonds is not a realistic option as it would result in a downgrading of the City's top AAA/Aaa bond ratings and the raising of future borrowing costs. It could also prevent the City from accessing the bond markets (to raise capital for City needs) for some period of time.

A second set of major issues for the City are the debt policy implications of the City issuing $275 million in new bonds to finance this new Metrorail station. For several decades the City has had in place very conservative debt policy guidelines with specific numerical targets and limits. This has resulted in the City's debt being considered low in comparison with other jurisdictions by the major bond rating agencies, Moody's Investors Service, and Standard & Poors. If the City issued $275 million in additional bonds it would increase the City's debt burdens in year 2015 and beyond by about 64% (from a projected $433 million in 2015 to $708 million). This would raise the City's primary measure of debt capacity (debt as a percent of property value) from a projected 1.18% in 2015 to 1.93%. In comparison with other AAA/Aaa rated localities in Virginia and Maryland this would shift the City's debt burdens from being on the low end when compared to those localities to the high end when compared to these peer localities.

While this represents a significant, material increase, according to the City's independent financial advisors, it would not in and of itself jeopardize the City's top AAA/Aaa bond ratings. In particular, the rating agencies recognize that the investment in heavy or light rail transit systems is an investment with multi-generational benefit if coupled with new transit-oriented development. This view and bond rating agency acceptance is highly likely to hold in the future, but cannot be guaranteed.

The issuance of $275 million in new debt will have the implication of potentially limiting future major public projects that the City may want to consider funding. For example, if federal, state or other funds are not substantially available to upgrade the planned Potomac Yard high-capacity transitway from a Bus Rapid Transit (BRT) to a street car system, then that upgrade may have to be delayed until such time as a large portion of the Metrorail station bonds have been repaid. The Metrorail and the high-capacity transitway are required to accommodate the traffic associated with the proposed development.